THE GAS COMMISSION OF MASSACHUSETTS.*

IN an earlier series of four articles† on "The Gas Supply of Boston," I sketched the financial and political history of the companies in that city. The logical conclusion from that narrative is that the relations of the companies to the investor, the public, the legislature, and the Commission, are not satisfactory. Since state action has not produced satisfactory results, it seems desirable to trace the underlying causes of this apparent failure. Let us ask, then, what evils have existed at the different stages of development, how these evils were regarded at the time by the public, what steps were taken to prevent and cure them as they arose, and how far and why such efforts failed of success.

Before taking up the history of the lighting companies in Massachusetts, it is desirable to make some general reference to similar companies in other parts of the country.

When it began to dawn on the public mind that competition in the gas business was no protection against corporate abuses and excessive charges, and when competition by the introduction of new processes and methods became so intense as to make the investment in this industry insecure, new relations had to be established between these companies and their patrons, on the one hand, and the companies and the public authorities, on the other. The consumers wanted good cheap gas, although their ideas of a reasonable price were necessarily vague;

* The legal title of this body since the Electric Light Companies were placed under its jurisdiction (Acts of 1887, c. 382) is "The Board of Gas and Electric Light Commissioners"; but, since I am here concerned with the board chiefly in its relation to the Gas Companies, I shall refer to it briefly as "The Gas Commission."

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and the companies wanted protection from competitors. The general public, so far as it had any views on the subject, believed that experience had demonstrated that gas must be supplied either by unregulated private companies or directly by public authority. Corporate managers had preferred, from the very beginning of the great development of the modern business corporation, to bear the expense of buying off competitors rather than to make known to the public the affairs of the companies. The undertakers of gas enterprises, for reasons already indicated, were no exception to this rule. They declared almost without exception that their companies were private undertakings, and could not legally or morally be subject to public control.

It must be admitted that the absence of any effective control in this country, as well as such legal decisions as existed, lent color to this view. Virtually, no administrative control was exercised over these companies by any American Commonwealth; while statutory limitations on the price of gas and the capitalization of companies were, except in Massachusetts, simply ignored. Rival companies so far had been the only weapon wielded in the supposed interests of the consumer. The direct fruit of such attempts was always the same,— over-investment and a rate war, followed by consolidation and unregulated monopoly, with prices usually sufficient to pay a dividend not only on the unnecessarily large investment, but also on the watered stock occasioned by the consolidation. The indirect outcome of such contests was generally a bitter hostility between corporations and those whom they served. It would scarcely be extravagant to say that each party had come to regard the other as an enemy to be exploited and injured as much as possible. One natural consequence of this method of procedure was that the companies tried to make very large gains in times of comparative calm to offset possible losses from future attacks of council or legislature.

This warfare had lasted so long that the public had lost confidence in the ability of the municipal governments, which at that time usually had the right of letting in or keeping out competing companies, to supervise or deal with the gas companies. In fact, the whole history of the relation of the cities to the companies in the past had proved that, in the matter of drawing contracts for public lighting, the companies nearly always overtopped the municipality and got the better of the bargain. With the exception of state inspection of the purity and quality of gas, and the testing of meters in Massachusetts since July 1, 1861,* the private citizen throughout the United States was left to make the best terms he could with the company. In regard to public lighting everywhere the cities often exacted from the companies such low prices as to make the prices for private lighting, under all the circumstances, necessarily high. A low price for public lighting was often made the condition of admitting a new company to a city. Even then there was constant friction between the companies and the public authorities in regard to the contracts for public lights. If, then, the cities were unable, even at the sacrifice of the interests of the private citizen, to make satisfactory arrangements with the companies for public lighting, it could scarcely be assumed that these same local governments, if given legal power, could exercise a wise and efficient supervision of the companies in the name of the state.

But one remedy for existing evils, therefore, seemed available; namely, to forsake traditional and instinctive feelings on the question of local self-government, and turn over the control of these companies to some organ of the Commonwealth. For at the time of which I am now writing the agitation for public ownership, while not by

*The title of this act is significant: "An Act for the inspection of gas meters, the protection of gas consumers, and the protection and regulation of gas light companies." The bill for this act was drafted by the president of the Boston Company. *Report of the Boston Gas Hearing of* 1867, p. 440.

any means unknown, was not strong enough to count as an important factor. It was also becoming increasingly plain to all but a few corporate managers that the public was not yet prepared to settle down calmly to uncontrolled private monopoly. The attitude of the managers of these companies towards what they regarded as interference with their private affairs had been such for many years as to render futile any attempt to control the companies until changed methods of production should increase the danger from competition. No revolutionizing discoveries were made in the industry until towards 1880; although even before this date the companies had been alarmed at times by the introduction of petroleum, and towards the end of the period were seriously threatened by the application of electricity to illuminating purposes.*

The two decades preceding the introduction of electricity and water gas make a peculiar period, during which the organization of competing companies in nearly all the states caused difficulties. But the companies were able to maintain almost complete secrecy, and, without any great changes in processes, to make increasing profits. This came about from the great fall in the price of materials for manufacture and plant, from many minor improvements in manufacture and choice of materials, together with an enormous increase in the demand for gas because of the increased well-being of a rapidly growing population, which was concentrating itself more and more about the gas companies. At the same time the increased consumption of gas made possible a much greater net gain from the residuals. Thus it was easy for established companies to carry the expense of driving out competitors and still distribute dividends as large as public sentiment would permit.

So long as the companies could maintain successfully

* The first electric lighting company was organized in Massachusetts in 1880, under the general law. *Second Annual Report of the Gas Commission*, p. 57.

the secrecy of their accounts, and continued to believe themselves entitled to all they could get out of the public, one of two results was sure to follow. They would either adopt the practice, almost universal outside of Massachusetts, of greatly over-capitalizing their investment, and thus distribute their total earnings without letting the public know the relation of their dividends to actual investment, or, as the majority of the larger Massachusetts companies did (in a measure restrained by statutes against stock-watering),—pay the maximum traditional dividend of 10 per cent., put their surplus into extensions of the plant, and, as it were, sleep. Truly, in such a typical case as that of the Boston Gas Light Company, to have had greater earnings would have been a genuine embarrassment; for the company was owned and managed by local residents of prominence, who did not care to violate the statutes by watering the stock. They dared not regularly distribute more in dividends. They had been able for years to meet their dividend charges and make extensions required by a rapidly growing population out of earnings.* There was no sign of a change in this particular as long as the selling price of gas remained relatively so high.

It did not seem wise to the management to call public attention to the great prosperity of the company by reducing prices to such a point as would probably give the same net income from much larger sales.† Until the public could acquire more knowledge in regard to the cost of

* During the fifteen years ending June 30, 1892, this company, with a share capital of $2,500,000, put $3,300,000 of its earnings into extensions, or at the rate of 9 per cent. of its capital stock per year. For the last three years of this period the surplus went largely to the Bay State Company. Hence it is fair to assume that the company was regularly meeting all its legitimate expenses and showing net gains of fully 20 per cent. per annum. See *Eighth Annual Report of the Gas Commission*, p. 255.

† The Gas Commission, in its *First Annual Report* (1886), page 16, remarks that "some companies have seemed to prefer a small consumption at a high price, assuring good dividends, to an increased consumption at a lower price with no greater dividends."

making and distributing gas, there seemed no particular occasion for agitation or complaint against this or similar companies. The management was honest, the prices, so far as the consumers knew, were reasonable, the dividends were not unreasonably high, and the company not only greatly under-capitalized, but known to be so.* This last fact, so far as the consumers were concerned, counted for much in an age of almost universal stock-watering. If the danger of competition could have been averted, the situation might have lasted indefinitely. For the rate of interest throughout the country was rapidly falling; and every increase in the investment under existing conditions, while not promising any addition to the amount distributed in dividends until the share capital could be increased, did apparently tend to make the increasingly handsome dividend of 10 per cent. more certain for a remote future.

Outside of Massachusetts the business was almost uniformly so profitable as to enable the companies in large cities to maintain high nominal dividends on an excessive capitalization. Generally speaking, the gas business before 1880, under old processes, was unusually profitable throughout the country, even after carrying the heavy expenses of buying up competitors. Furthermore, the companies appeared to be so thoroughly intrenched as to render useless any attempt to impose effective regulation upon them, even in Massachusetts. There was no public demand for regulation of the companies. Both the public and the companies were inclined to let well enough alone,

*The property of the Boston Company was valued by the tax assessors at $4,129,900 in 1886, while the total capitalization was but $2,500,000. *Second Annual Report of the Gas Commission*, p. 20.

That anti-stock-watering laws and sentiment in Massachusetts had not been without effect is further seen by the fact that in 1886 all the gas companies of the state were valued for purposes of taxation at $12,189,768; while their total capitalization (stock and bonds) amounted to but $11,731,850, nearly half a million less than the assessed valuation. *Third Annual Report of the Gas Commission*, pp. 19, 20.

and to jog along as they had been doing for so long a time. The public did not stop to consider how much more a 10 per cent. dividend in this industry meant in 1880 than in the days when that rate first came to be considered a fair one.

All this was changed very suddenly when the holders of water-gas patents, the makers of electrical apparatus, and the promoters of electric lighting companies, all swept into the field at the same time. In order to get control of the field, these advance-guards of industrial progress first made the air heavy with complaints about monopolies, extortionate prices, inadequate service, fabulous profits, and antiquated management. City councils the country over proved no match for the handful of aggressive and shrewd manipulators in control of the new processes.*

It is interesting to note that about this time the subjects discussed at the annual meetings of the various associations of gas manufacturers entirely changed. Competition occupied a prominent place in almost every meeting of this kind, and especially in the presidential addresses, for about a decade. The question before had been how to prevent state interference. It now became how to stimulate, direct, and control state interference so as to protect investments. The more far-seeing members of the associations recognized that the days of high charges and high profits, as measured by past standards, were gone forever, and that, if the companies wished to appeal to the state for protection, they must so manage their capitalization as to claim protection for "honest investments." They realized, also, that a request for protection would raise the cry of monopoly, which could be

* It will be recalled that the ultra-conservative managers of the Boston Company (who were no longer young in years) had apparently taken the precaution as early as 1880 to shut out water gas by statute. See this Journal, vol. xii. p. 426. A bill for a state gas commission was introduced into the legislature, and killed in committee in 1880. The companies had not yet made up their minds that they needed state protection.

safely met only by an acknowledgment of the state's right to regulate the monopoly in the public interest. Furthermore, the companies knew that this meant a high degree of publicity,* and that an impartial commission to act as arbitrator between the companies and the public was probably the best means of meeting the new needs of the companies. The idea was not a new one, for disinterested persons had suggested it years before. The remarkable thing was the suddenness and thoroughness with which the gas interests † embraced the suggestion after so completely rejecting it for so many years. So long as their enormous profits seemed perfectly secure, with so little effort on their part, the statement that the state ought to exercise control over the companies appeared absurd and even outrageous to them. The question now became simply how much of their previous claims the companies could afford to give up for the sake of state protection ‡ against rivals.

*Perhaps the most typical statement of the changed relations is to be found in the remarkable address of the late J. C. Pratt before the American Gas Association in 1882, entitled "The Future of the Gas Interests." *Proceedings*, vol. v. pp. 156–169. Mr. Pratt was not at that time a recent convert, — rather, a prophet. He served for thirty-six years as the head of the Jamaica Plain Company, and during all that time gave the financial statements prepared for his directors to the public. *First Annual Report of the Gas Commission*, p. 5.

Mr. Pratt spoke in similar vein before the same association in 1886. *Proceedings*, vol. vii. p. 232.

† The Choate Committee had recommended this form of control in 1877. See this Journal, vol. xii. p. 424. The presidents of the American Gas Association in their annual addresses took strong ground in favor of such a commission, in 1883 (Forstall), 1884 (Stedman), 1885 (Vanderpool), 1887 (Greenough), 1890 (Taber), 1892 (White), and 1894 (Pearson). In more recent years purely technical matters have occupied most of the time of these meetings. Nearly all the gas associations of the United States for years recommended state commissions for all the states. See the *American Gas Light Journal*, vol. xlv. pp. 5–7.

‡ From 1855 to 1870 the gas companies in Massachusetts under the general law enjoyed a statutory monopoly until they had paid more than 7 per cent. dividend for five years. See Statutes, 1855, c. 146, and 1870, c. 353. But, since there is no constitutional prohibition of special legislation in Massachusetts, the legislature could at any time introduce competing companies by special act.

The vacillating policy of the board of aldermen of Boston in the early eighties in regard to competing companies convinced the old companies in Massachusetts that they could not count on any protection from such sources. The moment that those in control of the water-gas patents gained confidence in their ability to make out a case plausible to the public, the contest between the old and the new under existing legal conditions became an unequal one. By 1884 the promoters of new enterprises had worked up enough sentiment against the existing order of things to occasion the organization of the Consumers' Company at Boston, and had themselves organized the Bay State Company. Before the legislature met, at the beginning of 1885, the first of these companies claimed * that it had the legal right to lay pipes in the street; and the council was wavering, so that it seemed likely to grant privileges in the streets to the Bay State Company.

The managers of the Boston Company still regarded the prohibition of water gas a bulwark against competition, and continued to regard the new processes as valuable for blackmailing purposes only. With all of their self-contented conservatism, however, they recognized that the popular mind had been worked up to a pitch which made legislation against existing companies probable. As a concession, therefore, to popular sentiment, those in control of the Boston field had the city government petition the legislature to create a board of state gas commissioners.†

It should be observed that, although the advocates of new methods and improved processes had, by more or less direct means, created some public feeling, yet the real struggle from now on was not between the public and the

* See this Journal, vol. xii. p. 424. On the basis for the claim of this company, see the opinion of Mr. E. R. Hoar, printed in the *Advertiser* of January 12, 1885.

† The city of Boston presented a similar petition to the legislature in 1867 as an alternative to threatened competition.

corporations, but between the old corporations and the new. This fact has a most important bearing on the later course of affairs. The petition for a state commission was approved by the city before either of the new companies gained admission to Boston, and while "a bitter struggle was impending with the Consumers' Company" in the council.*

The legislative committee to which this matter was first referred reported adversely on April 10, 1885. Although the Boston Company virtually drew the first bill,† the thing that company most wanted — namely, protection against competition — was not included in the first draft, but was introduced afterwards by representatives of the company.

Although the bill was hotly contested,‡ and debated at unusual length,— not less than thirteen set speeches being made on the motion to pass to the third reading in the House,— it was reasonably certain from the beginning that it would pass in substantially the form desired by the companies.

The Bay State Company got its rights in the streets before the bill became law. It was, perhaps, fortunate for the subsequent history of the Commission that the contest over its creation had been confined almost exclusively to the companies; for this gave the Commission time to organize and acquire knowledge before it was called upon to take any action on controverted points. For reasons made

*See p. 4, *Arguments of W. E. L. Dillaway before the Public Service Committee*, legislature of 1885.

† On the relation of the Boston Company to this bill, see the Boston *Advertiser* of February 21 and May 29, 1885, and the *Journal* of May 28, and the *Globe* of May 29. All the newspapers of prominence, except the *Globe*, supported the bill.

‡ The opponents of the bill stole a march at one stage, and by a vote of 80 to 57 struck out the clause limiting competition (Federhen amendment). Upon reconsideration this amendment was voted down by 73 to 55; while a similar amendment was lost in the Senate on June 2 by a vote of 5 to 22.

The act was approved, and went into effect June 11, 1885 (c. 314), entitled "An Act to create a Board of Gas Commissioners."

plain in the previous articles the two chief parties, the Bay State and the Boston Companies, did not care to bring any case before the Commission for some years; and the public took but little interest in its affairs. Both the great companies were disappointed: the old, that it did not get the Commission established before the other company was let in; the new, that the Commission was established at all. The other companies of the state, not realizing the extent of the impending revolution in the industry, had but little fear of reduction of price by the Commission, and were glad, on the whole, to have the prohibition of competition, although, perhaps, underestimating its importance.

The original act has not been essentially changed, except by constantly enlarging the powers, functions, and duties of the Commission. The Commission consists of three members appointed by the governor with the consent of the council for terms of three years, one going out each year. The commissioners are removable for cause only, and after a public hearing. The governor designates the chairman of the board, and with the consent of the council appoints a permanent clerk.

The Commission from the start was given general supervision of all the companies in the state, and required to see that they obey the law. In order to provide itself with the necessary information to enable it to carry out this provision, it is armed with practically unlimited inquisitorial powers.* The powers of this nature granted the Commission are much larger than have ever before been given in this country to any similar Commission dealing with industrial or financial interests. Upon the

* The original act gave the Commission the right to prescribe the form of the annual reports to be made by the companies. Upon the recommendations of the Commission, later acts allow the Commission to prescribe the methods of keeping the books and accounts of the companies, and even to require the companies to keep such station and distribution records as the Commission may direct. Acts of 1886, c. 346, and Acts of 1896, c. 480.

complaint in writing of the mayor or aldermen of any city or of the selectmen of any town, or of twenty consumers of any company, in regard to the quality or price of gas, the Commission may, after a public hearing, order such an improvement in the quality or reduction of the price as seems good to it.

Any interested party may appeal to the Commission from a vote of the local authorities either shutting out or letting in a competing company.* The decision of the Commission (after a public hearing) on such appeals is final. The Commission is required to report all violations of law on the part of the companies to the Attorney-General, and may apply directly to a court of equity † to enforce the law and all lawful orders of the board. The act also requires the Commission to make an annual report to the legislature, with recommendations of needed legislation.

It is fortunate that the powers of the Commission were no greater at the beginning, and that they have been enlarged from time to time as the Commission has felt its way and become better qualified to act wisely in a constantly widening field. Although the legislature has on several occasions, under the pressure of private interests and excited public opinion, acted contrary to the advice and better judgment of the Commission in regard to new legislation, it has never tried to interfere directly with the Commission by transferring or controlling its powers or compelling it to act or refuse to act in any particular manner.

No formal case was presented to the Commission for adjudication until it had been organized about a year and

* The local authorities are forbidden to vote to let in such competing company, except after a public hearing before them.

† By chapter 426, Acts of 1896, any justice of the Supreme Judicial Court or of the Superior Court is given equity jurisdiction in term time or vacation, upon the application of the Commission, to enforce any law or any lawful order of the Commission in regard to the supply of gas or electric lighting.

a half. Meantime it had made elaborate investigation on gas matters inside and outside the state, had got the reports of the companies into fairly good order,* and by personal visits to the works and managers of every company under its jurisdiction had exercised great influence on the accounts, over which at that time it had no compulsory powers. The First Report, 1886, deals largely with non-controversial matters, such as the necessity of uniformity of accounts and of fiscal years, accidents from gas, the theory of capitalization, the danger of allowing franchises to be leased or sold and of allowing companies to be managed entirely by non-residents.

The legislature attempted to embody in the act† of 1886 (c. 346) most of the recommendations of the Commission, and to prevent anticipated evils on the part of the Bay State Company.

In the Second Annual Report the Commission implied that in its own estimation it had already become the expert arm of the legislature in gas matters by saying‡ that it had not suggested any form of legislation, but that the commissioners stood ready to place any knowledge in their possession at the service of any committee of the legislature. In fact, the commissioners aspire to be not only the advisers of the legislature, but also general sources of disinterested information in all lighting matters. This is shown by the statement in the Seventh Annual Report§ that, "in addition to the duties imposed by the statute, it (the Commission) has been frequently consulted by city and town committees, managers, and in-

*That there is room for still further improvement in this particular may be inferred from the argument of Mr. G. W. Anderson in the Haverhill case, December 13, 1899, pp. 6, 7, pamphlet edition.

† The act forbade the leasing or sale of works or franchises, the issuing of bonds below par or in excess of the capital stock; authorized the board to compel service, placed individuals selling gas under the jurisdiction of the board, gave the Commission the right to inspect books and accounts, and fixed a uniform financial year for all the companies in the state.

‡ Page 58. § Page 3.

vestors in regard to questions concerning gas and electric lighting. Those interested in these matters have come to regard it as the most convenient source from which to obtain reliable information as to the standing and financial operations of the companies, and their relation to the local authorities, as well as in regard to many of the technical features of the business."

While it is doubtless possible for the Commission to overestimate its influence on legislation, and while it is beyond question that the legislature has at certain critical points ignored the advice of the Commission, it is certainly desirable that this advisory function should become a more and more prominent one. It is also plain that, if the Commission proves able to maintain its existence permanently, it must become a more and more important source of general information on lighting matters; for its opportunity of acquiring information capable of comparative use is not only unique, but is even greater than that of those actually engaged in the management of companies.

The Commission has met with but little direct opposition * from the companies, but has had great difficulty in getting the accounts kept properly and the annual returns to the Commission sent in promptly.† Probably the most important work of the earlier years consisted in getting the companies to keep their books and accounts in such a way that the managers themselves could know what they were about, and the Commission could use the reports of the companies for purposes of comparison. When this result had been reasonably attained, one of the greatest temptations to loose and dis-

*I have discovered, in the whole history of the Commission, but a single case where a company formally refused information to the board. That was a case in which the company was just ready to go into insolvency.

† The delay in making returns was partially checked when the legislature, upon the recommendation of the board, fixed a per diem penalty for such delay. Acts of 1891, c. 263.

honest management of companies disappeared; for it could not be supposed that such management could escape detection, and the certainty of being found out is always one of the greatest deterrents from unlawful or improper conduct of any kind.

But work of this kind, however important, is not apt to be highly appreciated by the public. In the beginning the Commission had but two powers likely to attract immediate favorable public notice,— those relating to price and to competing companies. So far as the people consciously expected benefit from the Commission, they probably looked for it from price reductions by direct order. Even this expectation was so vague as to overlook the fact that the power could not be exercised by the Commission upon its own initiative. Many of the criticisms passed upon the board in regard to price reductions show that the public even yet usually overlooks the fact that the Commission has no initiative at this point.

As a matter of fact, but few requests for reduction of price have been presented to the board. Many of these have been withdrawn before a decision was reached, because the company voluntarily met the original demands of the petitioners or effected some other satisfactory compromise. It is a striking fact, however, that in fifteen years the board has acted adversely on but two petitions for a reduction of price. In both of these cases the Commission seems to have justified its decision at the time to the petitioners.*

I believe it can easily be shown that the chief effect of the Commission on price has not only been an indirect

*The cases were those against the Cambridge and the Arlington Companies, both brought soon after the great agitation and legislative investigation of the Bay State Companies in 1893. The Cambridge Company had earned only a fair dividend on capital contributed by its stockholders, and carried a surplus which would, the board believed, enable it to make further voluntary reductions in price. It had already reduced its price by nine stages from $3.50 to $1.35 per thousand feet.— The Arlington Company, from the nature of its territory, could not expect large increase of sales from a reduction in price,

one, but has come largely from action in which the question of price was not a direct issue. Nevertheless, since we can best judge of indirect influence by a study of direct action, let us consider briefly some of the more important cases dealing directly with the price of gas.

The first important case of any kind brought before the Commission was a complaint presented January 4, 1887, by the consumers, against the quality and price of gas furnished by the Worcester Company. There could scarcely have been a case in which all the circumstances were more favorably arranged to enable the Commission to establish methods of procedure, and to lay down the general principles of government regulation by commission.

The Commission has from the beginning assumed that the state, in establishing a Commission, meant to obtain through regulated monopoly the benefits heretofore sought by competition.* According to this view, monopoly is a special privilege granted solely in the public interest. On this basis the protected monopoly is not entitled to charge more than is sufficient, with honest, progressive, and efficient management, to give a fair rate of income on the capital actually contributed by the stockholders. The doctrine of efficient management has been enforced in England for a generation, but was applied by this board for the first time in the United States.

and had never paid a fair dividend on the actual investment. The justice of the decision in this case is shown by the fact that the company failed and went into insolvency in March, 1899. *Tenth Annual Report*, pp. 12–14, 21, 23. *Fifteenth Annual Report*, p. 5.

During the present year the legislature has taken the initiative in ordering the Commission to consider the expediency of reducing the price of gas in both Lynn and New Bedford. In the first of these cases the decision (May 15, 1900) was against any reduction. In the New Bedford case (decided June 6, 1900) the board reduced the price slightly, and the company promptly accepted the decision.

*This view was confirmed by the Supreme Court in 1892, in the case of Attorney-General *ex rel.* Board of Gas and Electric Light Commission *v.* The Walworth Light and Power Company.

The Commission believed that, as the legislature in creating the Commission meant to introduce a new principle, so it intended also to break entirely with the old method of procedure. The old method was to proceed to enforce statutory provisions by means of the ordinary civil courts, with all their inevitable delay, expense, and technicality. It generally happened in such cases that all the important evidence was in possession of one party, with the burden of proof on the other. This system broke down more thoroughly, perhaps, at this point than at any other. The attempt to employ expert witnesses proved comparatively useless: first, because the only men whose knowledge justly entitled them to be called expert were too expensive for the plaintiff to employ as witnesses; second, because such men expected future permanent employment from the companies, and, therefore, would not incur their enmity by testifying; and, third, because, however much knowledge they might possess, it was generally knowledge of a different set of circumstances from those under consideration. The Commission, therefore, on the supposition that it was created in order that it might gather and become a depositary of a large body of comparative expert knowledge, acquired from every available source, refused to allow this first important case to turn on evidence furnished by the petitioners, who in such cases rarely have any accurate knowledge on the cost of making and distributing gas.

In addition, therefore, to taking all the evidence offered at the hearing in this as in all later cases, the board felt justified in making on its own initiative a most thorough examination into the history, policy, methods, and condition of the company from its organization.* This examination extended not only to the manufacturing and distributing plants, the station records, the books of account,

* In later cases the Commission has employed experts to make such an examination when that method seemed likely to furnish a sounder basis for judgment.

the corporate records, and the material on hand, but even to the services, pipes, burners, and fixtures in private buildings supplied by the company. In other words, the Commission, far from being bound by strict rules of evidence and procedure, applied to the case all the knowledge in its possession, including that obtained not only from years of study, but also from previous inspections of this and other companies, and from the sworn returns of every company in the state. The board was thus able to use its own previous knowledge as a general standard by which to measure the local circumstances in the particular case.

It appeared that the Worcester Company had from its organization — more than a generation ago — enjoyed an undisturbed monopoly in the second largest city in the Commonwealth, and had, during nearly the whole of this period, paid an annual dividend of 10 per cent. on its share capital, which had been fully paid in cash. The Commission found that the price was high and the number of consumers small for so large a city; that the total consumption was not more than a third to a half what it ought to be; and that, although the stock had never been watered, the capitalization was altogether too large for the output. The management was declared to be "narrow and illiberal," and the distributing system inadequate in extent and quality, even for the consumption of that time. The board recommended * very heavy expenditures for reconstructions and extensions, and a reduction of the price of gas from $1.80 to $1.50 net per thousand feet.

A few years later, and just after the company had voluntarily reduced the price from $1.50 to $1.40, the mayor

* The statute authorizes the Commission in such cases to *order* a reduction in the price. The uniform practice, however, has been in the first instance simply to recommend. Such recommendations were always accepted by the companies until the Haverhill Company, to which reference will be made later, rejected the recommendation of January 23, 1900.

In a few cases companies have petitioned for a rehearing, alleging changed circumstances or new evidence.

and aldermen of Worcester petitioned the board for a still further reduction of price. It appeared that, since the previous reduction by the board, the company, in carrying out the suggestions made in regard to reconstructions and extensions, had spent $350,000 without any increase of the share capital, which still stands at $500,000. By reducing the dividends,* the company had been able to put $250,000 out of earnings into these improvements, the remaining $100,000 being represented by outstanding bonds. The Commission, while commending the company for faithfully carrying out the earlier suggestions of the board, found still further expenditure for improvements necessary. It refused to sanction the idea of a stock issue for such purposes, declaring in this as in all other cases that "the ordinary demands which a progressive management desires and is bound to meet may fairly be provided out of income, when the price of gas is not made so high as to be burdensome." † In the face of all these facts, and notwithstanding the previous voluntary reduction of price and the already reduced rate of dividend and the existing debt, the board lowered the price once more to $1.25.

As will appear later, this theory of capitalization, which has been consistently adhered to by the board, leads inevitably in the case of growing companies to a large surplus; and such a surplus, after it reaches a certain limit, offers temptations, apparently irresistible, to capitalize it directly or indirectly.

Some of the peculiar difficulties of dealing with such a surplus, as well as some of the perplexities of determining what is a fair price of gas in the complexity of modern industrial conditions, will come out if we consider a few other typical petitions for a reduction of price.

* The first year after the reduction the dividend was but 6 per cent., the next year 6 1-2, and for the next seven years 8 per cent.

† *Tenth Annual Report*, pp. 31–33.

A case was brought against the Springfield Company in 1893. This company, while paying regular annual dividends of from 8 to 10 per cent., and carrying a steam-heating plant at a heavy loss, increased its capital stock from $50,000 to $450,000; and the subscribers paid for this new stock chiefly from the proceeds of extra dividends. The proceeds from the increase of stock were then, for the most part, put into extensions. That is, although there was no technical violation of law, the company in essence simply capitalized its surplus earnings from the sale of gas. The Commission recognized that the company, in maintaining the steam plant and capitalizing the surplus in this manner, had violated no law. But it could not see why the consumers of gas should be made to bear the burden of the loss on the heating plant; while the attempt to earn full dividends on the capitalized surplus, in the opinion of the Commission, was contrary to the policy of the state as understood by the Commission.

The theory of the Commission in regard to the surplus arising from the earnings of the company was, and is, that such surplus, being contributed entirely by the consumers, so far as it is not necessary as a sort of insurance fund to guarantee future dividends on the original capital contributed by the shareholders and to enable the company to make future reductions of price, has no reason to exist, and has been taken from the consumers by an unjust price. It follows, therefore, that, although a surplus of this kind belongs legally to the shareholders, the consumers, in the eyes of the Commission, are entitled to share in its benefits. Following such reasoning, the board fixed the price at $1.40 net,* thus penalizing the company for capitalizing its surplus. The board expressed the opinion that the price fixed would require either "a substantial increase of business" or a reduction in the dividends.†

* The price had been $1.65, with special discounts to very large consumers.

† *Ninth Annual Report*, p. 9. For fifteen months after the decision the

In this case the surplus had already been indirectly, but legally, capitalized before the case was begun. On the other hand, the petition against the East Boston Company (1893) was virtually a petition of the consumers for an interest in the as yet uncapitalized surplus of about 35 per cent., one-half of which was invested in extension, the other half in interest-bearing securities. There had been no violation or evasion of law, dividends had been moderate, the management had been friendly and efficient, and prices had heretofore been considered just for both the public and private lighting. In fact, the prices for the public lighting had usually been the same as those charged by the neighboring Boston Company in very much richer territory.

In the opinion of the Commission the surplus was chiefly due, under good management, to relatively fixed prices somewhat lower than those charged by other companies similarly situated, in a community rapidly growing in wealth, population, and industry. Since there is no legal limitation of dividends, the Commission could not deny the legal right of the company to distribute this surplus in the form of dividends; but it declared that such a policy would probably prove fatal to the prosperity of the company. Therefore, on the basis of the principle already laid down, to the effect that the surplus is for the joint benefit of the consumers and the company, the Commission reduced the price from $1.75 gross to $1.50 net per thousand, with the statement that the surplus would insure the company against hardship in case the reduced price failed to bring sufficient increase of sales to maintain the dividend.*

Two cases against the Chelsea Company present some

company maintained its usual rate of dividend,—8 per cent.,—but since that has paid but 6 per cent. annually.

* *Ninth Annual Report*, pp. 9–11. The company has maintained a 10 per cent dividend rate since, with the exception of the single year 1897, when it paid but 9 per cent.

new and interesting points of view. In 1890 the board reduced the price charged by this company to $1.80 (with a special rate of $1.75 for large consumers), and suggested the desirability of a reduction in the dividend, which had been at the rate of 6 per cent. This decision rested on the fact that an earlier management had, although keeping within the law, over-capitalized the company, and that the present management, while honest, was inefficient. When, three years later, the second case against this company was heard, it appeared that the previous reduction of price had not greatly increased the sales, and that profits, but not the dividend rate, had somewhat decreased. The board fixed a uniform rate of $1.65 per thousand.

Shortly thereafter the company petitioned * for a rehearing of the case, setting forth: (1) a heavy loss by fire since the decision; (2) a large dropping off in sales, due to the business depression; (3) the necessity for more expensive improvements than were foreseen at the time of the decision; (4) a probable saving of expense, if a discount for prompt payment should be allowed; and, finally, (5) that the rate of dividend had already fallen to 5 per cent. The case was reopened; and, as a result, a maximum price of $1.70 per thousand on all bills paid by the 25th of the month in which they are presented was approved. The Commission did not anticipate that such a price would yield more than 5 per cent. dividend. In the long run this expectation was justified. The company raised its dividend rate for that year to 6 per cent., but since that date has never paid in any one year more than 5 per cent., averaging about 4¼. This low rate of dividend was

* The petition was brought under chapter 350, Acts of 1888. It was not until this act was passed that a company could initiate proceedings before the board to determine the price of gas. The price fixed by the board upon petition of a company cannot thereafter be changed except by the consent of the board. By the same statute a price fixed by the board, upon a petition of the consumers or the public authorities, cannot be *raised* without the consent of the board. It would appear that, when a price has been fixed at the request of a company, the company is thereby prevented from selling below cost.

brought about by the Commission when there was no charge of dishonesty or stock-watering, but on the sole ground of excessive capitalization, caused by improvident and injudicious management, chiefly at an earlier date, by a different set of managers.

The case of the Charlestown Company (1894) presented a genuine example of stock-watering. The stock in question was put out to represent "the supposed increased value of the plant" before the statutes forbade such issues. During the first fifteen years of its existence the company, notwithstanding the water in its stock, paid 8 per cent., and for the remaining twenty-seven years 10 per cent. annually. The Commission, in the belief that, under such circumstances, the rate of dividend ought to be reduced and the burden of necessary improvements placed upon the stockholders, fixed the price at $1.40, when bills are paid promptly. The result of the decision was to reduce the annual dividend for the next three years from 10 to 6 per cent.

One of the most striking cases in regard to price was that against the Brockton Company in 1895. Through speculative management, improper leases, and absurd, if not dishonest, expenditure for patents (under arrangements entered into, however, for the most part before such practices were prohibited by statute), the company had been greatly over-capitalized. It was, nevertheless, paying about 6 per cent. annually on all its stock ($178,500) and bonds ($100,000). The board reduced the price of gas 28 per cent., to $1.50, on the supposition that such a price would give a fair return on *the cost of duplicating* the plant. The board declared that "the burdens of reckless management belong to the corporation, and not to the public," and "that the profits of companies supplying this kind of public service must compare favorably with those which a new company might need to pay a fair dividend, when fully equipped to render the same service." * This de-

**Eleventh Annual Report*, p. 14.

cision went into effect at the beginning of the fiscal year 1895–96, and since that time the company has not declared any dividends.

In 1896 the Commission reduced the price charged by the Malden and Melrose Company from $1.60 to $1.50 per thousand feet, on the sole ground that the company had "failed to attain a high standard of efficiency," and in order to "compel the company to employ the strictest economy and the highest technical skill." This company had not only not watered its stock, but had actually issued about one-third of it "at a price much above par," and had rarely exceeded a 6 per cent. dividend. It may be inferred that the decision had the desired effect, as the usual rate of dividend has since been maintained.

By far the most interesting cases involving the question of price and surplus were those against the Haverhill Company. This company had always had a monopoly, and had always been well managed. Since 1871 it had had a share capital of $75,000 and a constantly growing surplus. On July 1, 1894, the Commission reduced the price from $1.40 to $1.30 per thousand, on the ground that the company already had a surplus of about $132,000, with an income more than sufficient to make all needed extensions and pay its regular dividend of 10 per cent. The Commission especially commended the "honorable record of the company," and, reiterating its well-established views on extension and surplus, said: "Everything which the company under discussion has taken in the past from its customers, except the cost of manufacture, including regular dividends upon its capital, is to-day existent and used for the benefit of its consumers. The stockholders from all this increase receive only a practical guaranty of a 10 per cent. dividend."

Those in control of the company did not propose to see its great surplus disappear at the hands of the Commission, nor to accept $7,500 yearly as a satisfactory com-

pensation for the use and management of a property already worth about a quarter of a million dollars, and constantly increasing in value with the rapid growth of the city. The directors, after allowing the surplus to increase for two years more, braved public opinion, and for the years 1897–99 paid extra dividends of 3, 40, and 10 per cent. respectively. Knowing that such dividends meant appeals for further reduction of price, the owners in June, 1899, undertook to realize on the surplus in another way. They sold the stock outright for $500,000 cash to the Haverhill Gas Securities Company, organized under the general laws of Massachusetts, apparently for no other purpose than to make a profit from the surplus of this gas company. The promoters of the Securities Company first got an option on the stock of the gas company, then organized their company, paying its capital stock ($500,000) in cash. They next paid this cash for the stock of the gas company. Thereupon they issued a 5 per cent. loan of the Securities Company for $500,000, putting all the property, franchises, and stock of the gas company in trust * to secure the loan. It is to be presumed that the proceeds of the loan went to replace the $500,000 originally subscribed for the stock of the Securities Company,† leaving the bondholders of the Securities Company the only persons with any money invested in the enterprise; while the shareholders of the Securities Company had the exclusive management of the property. The tangible property of the gas company was estimated in this sale at $425,000, and the good will at $75,000.

In the Fifteenth Annual Report (1900), pp. 6–8, the Commission condemned this whole transaction as "a defi-

* On the question of the legality of this deed of trust under the Act of 1886, c. 346, and the anti-stock-watering acts of 1894, see pp. 26–36 of the argument of Mr. G. W. Anderson, referred to above, p. 521.

† Provision was made for a possible additional loan of $100,000 for extensions of the gas-works.

ance of what for more than thirty years has been the well-understood policy of the state toward such corporations," and recommended that the legislature forfeit the charter of the Securities Company. Almost as soon as the existence of the Securities Company became known, the City of Haverhill asked the Commission to reduce the price of gas. The price already stood at $1, the minimum ever reached by any company in the state, save during the stress of actual competition. Because of the relative largeness of the surplus, the speculation based upon it, the recent large extra dividends, the already low price, and the uniform rulings of the Commission on the question of surplus, the case was truly a remarkable one. The board, having in the earlier case specifically ruled on the equitable disposition of this particular surplus, and having previously condemned the Securities Company for trying to evade that ruling, was virtually compelled to maintain its previous ruling, and to fix a price that would strike a blow at the Securities Company. No half-way measure was possible. The price was fixed at 80 cents per thousand after February 1, 1900. The company promptly appealed to the courts against this action of the Commission, on the ground that the price named was unreasonable.

Whatever the outcome of this legal contest, the prestige of the Commission is likely to suffer. The Commission and the legislature, as a result of this ruling, are fairly overwhelmed with petitions for price reductions. The politicians and the voters generally in all the larger cities are not likely to consider the amount, origin, or significance of a surplus, but to demand gas as cheap as the people of Haverhill get it. Should the Commission be sustained by the courts, the pressure for a reduction of the price charged by companies less favorably situated must therefore become almost, if not quite, irresistible. On the other hand, if the court decides against the Commis-

sion, the people will lose confidence in the judgment of the Commission, while every company will contest or threaten to contest official price reductions.

Although the Commission has on one or two occasions intimated * that accumulated earnings may possibly be permitted to earn dividends at a reduced rate, it has never for a moment admitted the justice of a higher rate than 10 per cent. on the capital contributed by the shareholders. Its rulings on extensions and on surplus clearly commit it to a non-capitalization of profits and the making of extensions out of earnings. Without predicting how the court will decide this or any other particular case or expressing an opinion on the justice of the ruling of the Commission in the Haverhill case, I think it safe to say that, where so large a surplus as that of the Haverhill Company or of the Boston Company has been lawfully acquired, the owners will, in one way or another, realize an income out of it in spite of any commission or statutes. The evil is done — if it is an evil — when the surplus has been created; and, until American governments are much stronger than they now are, it is at least doubtful if any administrative body can wrest from its legal owners by price reductions so large a surplus as this, or if to do so is not to punish one set of owners for the supposed misdeeds of another set.

The foregoing account serves to make plain the origin of the Commission, and sufficiently illustrates the theory which has governed its action in regard to the price of gas.† We have seen that almost every petition for a reduction of the price has been acted upon favorably by the Commission, and that the reductions, in accordance with the expectations of the Commission, have usually reduced or even destroyed dividends. This indicates that the

* See the *Ninth Annual Report*, p. 8, and the *Tenth Annual Report*, p. 23.

† The peculiar characteristics of the reductions in the case of the Bay State and Brookline Companies should be recalled at this point. See this Journal, vol. xiii. pp. 300 and 307.

Commission has had an important direct effect on the price of gas in the cases brought before it. Such a policy must have had a great effect, also, in causing voluntary reductions and in preventing action of any kind on the part of the companies likely to call forth petitions for price reductions. It goes almost without saying that temptation to over-capitalization will disappear if it ever becomes clear that the Commission has the inclination and the power to prevent the payment of dividends on an excessive capitalization. In the light of the above facts, it can scarcely be questioned that the indirect influence of the Commission on the price of gas exceeds the direct effects. A good commission, like a good police force, is chiefly valuable for the evil its very existence prevents, without any action whatever on its part.

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